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SUBJECT: UAE STOCK MARKETS' DOWN AS LIQUIDITY DRIES UP

Classified By: Ambassador Michele J. Sison for reasons 1.4 (b & d).

¶1. (SBU) Both of the UAE's domestic stock markets have dropped in value sharply since the beginning of the year. Dubai's stock market dropped by five percent on March 13 to its lowest point in 11 months. Abu Dhabi's stock market dropped by about two and a half percent on the same day. Dubai's market is now down by over 30 percent and Abu Dhabi's is down by almost twenty percent since the start of the year.

Two large IPOs have sucked liquidity out of the stock markets as investors sell holdings to buy shares in two companies (UAE mortgage house Tamweel and the UAE's second telecom service%mq6

¶2. (SBU) Two financial analysts told econchief that there were several causes for the drop in price. The most important reason was the intense interest in the above IPOs. In addition, however, they noted that both the Dubai and Abu Dhabi stock markets had finished 2005 significantly overvalued and were due for a "correction." One noted that many of the Arab markets were seeing a correction, citing recent protests in Jordan and Kuwait over drops in market prices. They both argued that the UAE's markets were now much more reasonably priced, if not relatively cheap. They stressed that most companies' fundamentals and profitability were good. One commented that banks such as Abu Dhabi Commercial Bank and National Bank of Abu Dhabi were both undervalued, and that he was recommending that his clients buy. He admitted that the stock markets were not likely to increase in value by 40 percent, but commented that a 10 percent increase was doable and "good money."

¶3. (SBU) Both analysts stated that there was a feeding frenzy for the two IPOs, with investors selling shares to participate in what would be oversubscribed IPOs. They explained that there were other factors pushing the stock market prices down as well, including some selling by UAE mutual funds that had reached their lower price limits, and a certain market hysteria. One noted that herd behavior applies to selling as well as buying. One analyst also stated that the UAE stock markets lack credibility, explaining that the Securities and Commodities Authority (the regulator) shared board members with the stock exchanges, and that these board members also owned companies and brokerage houses which, he said, raised the risk of insider trading.

¶4. (C) Consul General Dubai asked Minstate for Cabinet Affairs (and Dubai Holdings chairman) Mohammed Gergawi how he explained the recent crash in stock prices (at the time of the conversation -- mid-day -- Dubai prices were down an additional ten percent). Gergawi said a big part of the problem was the lack of long term investors. "In our young, immature market, nearly all the investors are day traders." Another big problem, he said, was "insider trading." Gergawi said he had recently counseled Minister of Economy Lubna Al

Qassimi about the need to "completely update" the UAE's trading laws, with the aim of providing greater transparency. "I told her to study the laws in the U.S. and Britain and pattern our new law after that," Gergawi said.

15. (SBU) Comment: Sharp inflows of capital over the last few years have contributed to strong UAE economic growth. They also contributed to a sharp increase in the stock market capitalization with share prices that many observers thought were higher than market fundamentals would justify. Both markets are still relatively illiquid (few tradable shares) as reflected by the sharp drop in market indexes as participants rush for two large IPOs. End Comment.
SISON